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In the Supreme Court of the United States

OCTOBER TERM, 1987

OTIS R. BOWEN, SECRETARY OF HEALTH AND HUMAN SERVICES, PETITIONER

v.

GEORGETOWN UNIVERSITY HOSPITAL, ET AL.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

REPLY MEMORANDUM FOR THE PETITIONER

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TABLE OF AUTHORITIES

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1. Respondents argue (Br. in Opp. 5-7) that review by this Court is unwarranted because this case is "unique"; they assert that the Secretary has for the "first and only time" attempted to use the rulemaking process to "reverse a lower court judgment" (Br. in Opp. 5). Respondents' contention rests upon a wholly distorted view of the issues in this case.

The Secretary's 1981 rule governing Medicare reimbursement for hospital wage costs was invalidated on procedural grounds in *District of Columbia Hospital Ass'n* v. *Heckler*, No. 82-2520 (D.D.C. Apr. 29, 1983). The district court in that case refused to issue an order barring the Secretary from applying the 1981 rule to respondents' reimbursement claims, holding that the provisions of the Medicare statute requiring exhaustion of administrative remedies deprived the court of the authority to issue such

an order. The court expressly stated that respondents' reimbursement claims were left to be adjudicated in the administrative process. Pet. App. 62a-64a. As its terms make clear (see *id.* at 64a), the 1983 order simply invalidated the 1981 rule; it did not address the Secretary's authority to (1) issue a new rule to govern the reimbursement question that would have been covered by the 1981 rule, and (2) apply any such new rule to respondents' reimbursement claims.

Indeed, respondents' argument here is identical to the argument that this Court rejected in *SEC* v. *Chenery Corp.*, 332 U.S. 194 (1947). Previously, in *SEC* v. *Chenery Corp.*, 318 U.S. 80 (1943), the Court had invalidated an order of the Securities and Exchange Commission imposing a condition on the approval of a utility reorganization plan and directed that the case be remanded to the Commission for further proceedings. The Commission on remand "reexamined the problem, recast its rationale and reached the same result" (332 U.S. at 196). The respondents argued before this Court that the Court's prior decision foreclosed the Commission from again reaching the same result. They contended that "the Commission would be free only to promulgate a general rule [imposing such conditions upon] utility reorganizations; but such a rule would have to be prospective in nature and have no retroactive effect upon the instant situation" (*id.* at 199-200).

This Court squarely rejected the respondents' argument. The Court stated that its prior decision held "no more and no less than that the Commission's first order was unsupportable for the reasons supplied by that agency. But when the case left this Court, the problem [addressed in the Commission's order] still lacked a final and complete answer" (332 U.S. at 200). The Court explained that "[t]he

fact that the Commission had committed a legal error in its first disposition of the case certainly gave [the respondents] no vested right to receive the benefits of [an order approving the reorganization without the condition]. * * * After the remand was made, therefore, the Commission was bound to deal with the problem afresh, performing the function delegated to it by Congress" (*id.* at 200-201). The Court went on to hold that retroactive application of the new legal rule was proper on the facts of that case (*id.* at 202-209).

Here, the district court's 1983 order did not finally decide the question of the appropriate standard to be applied in calculating wage cost reimbursement owed to respondents under the Medicare program. The district court's order, like this Court's order in the first *Chenery* case, simply rejected—on procedural grounds—one answer to that question. The Secretary retained his otherwise-existing authority to "deal with the problem afresh, performing the function delegated to [him] by Congress." The question in this case, therefore, is whether the Secretary's decision to apply the 1984 rule retroactively to cost reports that would have been governed by the 1981 rule falls within the rulemaking authority delegated to the Secretary by Congress. Like this Court's order in the first *Chenery* case, the district court's 1983 order is simply not relevant to that question.[1]

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[1] Respondents emphasize (Br. in Opp. 5) their contention that the Secretary seeks to recoup funds previously paid to respondents. First, contrary to respondents' assertion, respondents were not paid pursuant to a court order. They were paid pursuant to the Medicare cost reimbursement procedures, which were not the subject of the district court's order. And those payments were expressly made subject to reopening and recoupment in the event of an adjustment in

2. Respondents dispute our contention (Pet. 13-15) that there is a conflict among the courts of appeals with respect to the Secretary's authority to issue retroactive rules under Section 1861(v)(1)(A)(ii) of the Medicare Act, 42 U.S.C. (Supp. III) 1395x(v)(1)(A)(ii). Nevertheless, respondents appear to agree that the courts of appeals have reached differing conclusions about the meaning of this provision. Indeed, because those courts have themselves acknowledged the conflict (see Pet. 15 n.8), respondents would be hard-pressed to deny it. Respondents instead assert that the conflict is not presented in this case for two different reasons.

Respondents first observe that the present case involves a retroactive cost limit rule and argue (Br. in Opp. 15-16) that, because the decisions of the courts of appeals interpreting Section 1861(v)(1)(A)(ii) to authorize retroactive rules of general application were rendered in cases in which cost reimbursement rules of general application other than cost limit rules were at issue, those decisions are distinguishable from the present case. Respondents' distinction simply makes no sense. Nothing in the text of Section 1861(v)(1)(A)(ii) ties the scope of the Secretary's authority under that provision to the type of cost reimbursement standard to be applied retroactively. Section 1861(v)(1)(A)(ii) grants the Secretary the authority to promulgate regulations for "the making of suitable retroactive

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the amount of reimbursement as the result of the adoption of a new wage cost regulation. See, *e.g.*, Letter from R.M. Hugney to Robert B. Johnson (Jan. 31, 1984); 42 C.F.R. 405.1885.

Respondents express (Br. in Opp. 6-7) great surprise that the Secretary would choose to issue a new rule rather than appeal the district court's order. It surely is not a novel proposition that an administrative agency may decide to conduct a new rulemaking to cure a defect found by a district court instead of seeking appellate review of the adverse decision.

corrective adjustments" in reimbursement awards, without in any way limiting that retroactive authority to certain types of cost rules.

Simply put, Section 1861(v)(1)(A)(ii) does one of three things. Either it authorizes the Secretary to issue regulations of general application to be applied retroactively in individual reimbursement cases, or, as the court of appeals concluded, it is limited to empowering the Secretary to conduct a case-by-case reassessment of the reasonableness of particular reimbursement awards, or it authorizes a case-by-case reconciliation of advance estimated payments with the final reimbursement award. The statutory language does not admit of a distinction between different types of cost regulations. Since some courts have concluded that the statute permits the issuance of retroactive regulations of general application and other courts have concluded that it does not, there plainly is a conflict in interpretation warranting review by this Court. *E.g.*, compare *Springdale Convalescent Center* v. *Mathews*, 545 F.2d 943, 954 (5th Cir. 1977) (generally construing Section 1861(v)(1)(A)(ii) to authorize issuance of retroactive regulations) and *Tallahassee Memorial Regional Medical Center* v. *Bowen*, 815 F.2d 1435, 1453-1454 & n.36 (11th Cir. 1987), petition for cert. pending, No. 87-380 (applying balancing test to determine whether rule may be applied retroactively under Section 1861(v)(1)(A)(ii)) with Pet. App. 16a-19a (Section 1861(v)(1)(A)(ii) does not authorize issuance of retroactive rules of general application); see also Pet. 13-15.[2]

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[2] Respondents suggest (Br. in Opp. 9-11, 12) that what they refer to as "section 223(b)" independently bars the issuance of retroactive cost limit regulations. As an initial matter, we note that this is not a separate statute or even a separate section of the Medicare Act. It is simply a section of the 1972 amendments which adds a phrase to the

Indeed, the court below neither limited its construction of Section 1861(v)(1)(A)(ii) to the cost limit context nor relied upon any peculiar characteristic of cost limit rules to justify its conclusion about the limited scope of Section 1861(v)(1)(A)(ii) (see Pet. App. 16a-19a). The court's in-

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third sentence of Section 1861(v)(1) of the Medicare Act authorizing the issuance of cost limit rules (see Br. in Opp. App. 70(a)). In any event, as we explained in the petition (at 16-17), any restriction imposed by that provision is not applicable here. Respondents' contrary argument (Br. in Opp. 10-11) consists of the citation of statements that various cost limit rules would be prospective in effect; respondents cite no statement by the Secretary that the statute bars the issuance of a cost limit rule that is retrospective in the limited sense of the rule at issue here (see Pet. 11-13).

In any event, this purported distinction provides no aid to respondents' effort to explain away the conflicting decisions of the courts of appeals because no court has relied upon that alleged distinction in interpreting Section 1861(v)(1)(A)(ii) in the cost limit rule context. In *Mason General Hospital* v. *Secretary of Health & Human Services*, 809 F.2d 1220 (6th Cir. 1987), a case concerning the retroactivity of the Medicare malpractice insurance rule, which is not a cost limit rule, the court cited the legislative history of the cost limit provision relied upon by respondents and concluded that a balancing test should be used to determine whether a retroactive rule of general application may be issued under Section 1861(v)(1)(A)(ii) (see 809 F.2d at 1224-1226). The one court that has addressed respondents' contention has thus found that retroactive rules of general application may nonetheless in some circumstances be authorized by Section 1861(v)(1)(A)(ii).

Furthermore, as we discuss in our petition (at 14-15), some courts have concluded that Section 1861(v)(1)(A)(ii) does not permit any retroactive alteration in reimbursement standards, but simply authorizes the Secretary to carry out a bookkeeping reconciliation between advance estimated payments to a provider and the amount of reimbursement actually found to be owing to the provider. The distinction relied upon by respondents does not explain this division of opinion among the courts of appeals. Review of this question of statutory interpretation is therefore appropriate in this case.

terpretation of Section 1861(v)(1)(A)(ii) by its terms extends to all cost reimbursement standards, not just cost limit rules. Since the court below did not write the narrower opinion postulated by respondents, respondents have plainly failed to distinguish the conflicting decisions of the other courts of appeals.[3]

Respondents also assert (Br. in Opp. 16-17) that the decisions of the other courts of appeals upholding retroactive rules are distinguishable because those courts relied upon the "limited retroactivity" of the rules under review. But the court below did not hold Section 1861(v)(1)(A)(ii) inapplicable because of the degree of the rule's retroactivity; it concluded that the provision does not authorize *any* retroactive rules of general application. Moreover, as we discuss in our petition (at 11-12) the retroactivity of the rule at issue here was quite limited: the governing standard was published before it was placed into effect. Since the rule at issue here is therefore retroactive in a formal sense, but could not by its nature upset the reasonable expectations of entities subject to the rule, the decision below squarely conflicts with the decisions of the other courts of appeals.[4]

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[3] Moreover, respondents' own argument regarding the proper interpretation of Section 1861(v)(1)(A)(ii) does not distinguish between cost limit regulations and other types of regulations, but rather contends that the provision authorizes only case-by-case reexamination of reimbursement awards, not retroactive regulations of general application. See Br. in Opp. 12-14. Indeed, respondent appears to endorse an interpretation of Section 1861(v)(1)(A)(ii) more restrictive than that adopted by the court of appeals. Compare Br. in Opp. 13-14 with note 2, *supra*.

[4] We addressed in the petition (at 15-16 n.9) respondents' contention (Br. in Opp. 11) that the Secretary did not properly invoke Section 1861(v)(1)(A)(ii) to justify the promulgation of the rule at issue here.

3. Respondents argue (Br. in Opp. 19) that the question presented in the petition regarding the effect of the Administrative Procedure Act (APA) upon the Secretary's authority to issue retroactive rules is not properly raised in this case, but their contention ignores the opinion written by the court of appeals. Specifically, respondents contend that the Medicare statute itself prohibits the promulgation of a retroactive cost limit rule and that the Court therefore need not consider whether the APA also barred the issuance of the rule. But, as far as we are aware, no court has ever endorsed the contention that the Medicare statute bars the promulgation of retroactive cost limit rules. And the court below plainly did not rest its decision upon that ground; to the contrary, it held that the Medicare statute does not specifically authorize retroactive cost limit rules. In view of the considerable practical importance of the issue that the court of appeals *did* decide (see Pet. 24-25), respondents' assertions about the meaning of the Medicare statute provide no reason for this Court to decline to review that question. See also Pet. 16-17 (addressing argument that the Medicare statute bars retroactive cost limit rules); note 2, *supra* (same).

Respondents also list (Br. in Opp. 21-22) five facts that they assert distinguish the court of appeals' decision in this case from the decisions in which other courts of appeals have stated that the APA does not bar the issuance of retroactive rules. Unfortunately for respondents, none of these facts was relied upon by the court of appeals in the present case, and none of the other courts relied upon the absence of those facts in holding that retroactive rulemaking may be permissible. For that reason, they do not serve to distinguish the conflicting decisions of the other courts of appeals.[5]

[5] Respondents' disputation (Br. in Opp. 19-21, 23) about the merits of the APA issue merely confirms that there is a disagreement about an important issue of statutory construction warranting this Court's attention. We note that respondents fail to provide any reason why the APA should be interpreted to bar the adoption of rules having a retroactive effect when, as even the court of appeals recognized (see Pet. App. 11a-13a) the statute plainly permits retroactive application of new legal principles in the adjudicatory context. This is especially true when the language of the statute and its legislative history plainly point to the conclusion that retroactive rules are permissible in appropriate circumstances (see Pet. 19-22).

4. a. Respondents do not dispute that the question presented regarding the court of appeals' construction of the APA is an issue of considerable practical importance. See Pet. 24-25 (discussing importance of the APA issue). They do argue, however, that the question regarding the proper construction of Section 1861(v)(1)(A)(ii) has no continuing importance. But Medicare cost reimbursement rules are applied on an ongoing basis to a large number of providers of health services (see Pet. 23-24). Respondents themselves concede that cost limit rules currently apply to a variety of providers (the Department of Health and Human Services informs us that these providers receive more than $3 billion in reimbursement annually); and respondents' statement that no such rules currently apply to hospitals does not mean that such rules may not be adopted in the future. Finally, as we have discussed, the question presented regarding the scope of Section 1861(v)(1)(A)(ii) is not restricted to cost limit rules; the same statute governs the Secretary's authority to adopt other retroactive cost reimbursement rules. The court of appeals has thus limited the Secretary's authority to administer a program involving a substantial amount of federal resources. This issue is therefore of sufficient importance to warrant this Court's attention. See *Bethesda Hospital Ass'n* v. *Bowen*, cert. granted, No. 86-1764 (Oct. 5, 1987) (case in which the Court recently granted cer-

tiorari to consider another question involving the Medicare cost reimbursement system).[6]

b. Respondents also assert (Br. in Opp. 23-25) that the court of appeals' judgment can be supported on a variety of alternative grounds. Respondents will, of course, be free to raise before this Court any alternative arguments presented below. In view of the importance of the questions decided by the court of appeals, however, these alternative arguments should not deter the Court from granting review in this case.[7]

For the foregoing reasons, and the reasons stated in the petition, it is respectfully submitted that the petition for a writ of certiorari should be granted.

DONALD B. AYER*
Acting Solicitor General

FEBRUARY 1988

[6] Respondents question (Br. in Opp. 18-19) our statement that many pending cases involve challenges to the Secretary's authority to promulgate retroactive cost limit regulations (see Pet. 24. n.15). We were referring to the several hundred cases involving challenges to the retroactive medical malpractice reimbursement rule which, although they technically do not involve a cost limit regulation, present virtually the same question regarding the scope of Section 1861(v)(1)(A)(ii) as the present case. The Secretary has issued a settlement offer with respect to these cases, but it is not possible to determine whether the offer will be accepted by any of the many thousands of parties to those cases.

[7] Only one of these arguments was considered by either of the courts below. As we discuss in the petition (at 22-23 n.13), the district court plainly erred by concluding that retroactive application of the 1984 rule was impermissible under the balancing test set forth in *Retail, Wholesale & Dep't Store Union* v. *NLRB*, 466 F.2d 380 (D.C. Cir. 1972).

* The Solicitor General is disqualified in this case.

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